

Amend 2 Cal. Code Regs. Section 18705.1 to read:

§ 18705.1. Materiality Standard: Economic Interests in Business Entities.

(a) Introduction.

(1) If a business entity in which a public official has an economic interest is directly involved in a governmental decision (see ~~Cal. Code Regs., tit. 2, section~~ Regulation 18704.1(a)), use the standards in subdivision (b) of this regulation.

(2) If a business entity in which a public official has an economic interest is indirectly involved in a governmental decision (see ~~Cal. Code Regs., tit. 2, section~~ Regulation 18704.1(b)), use the standards in subdivision (c) of this regulation.

(b) Directly involved business entities.

(1) General Rule: Unless the exception in subdivision (b)(2) of this regulation applies, the financial effects of a governmental decision on a business entity which is directly involved in the governmental decision is presumed to be material. This presumption may be rebutted by proof that it is not reasonably foreseeable that the governmental decision will have any financial effect on the business entity.

(2) Exception: If the public official's only economic interest in the business entity is an investment interest (see ~~Government Code section~~ Section 87103(a)), and the public official's investment in the business entity is worth \$ 25,000 or less, ~~then~~ apply the materiality standards in either of the following provisions, as applicable:

(A) subdivision Subdivision (c)(1) of this regulation if the business entity is listed on in the Fortune 500, or if not listed in the Fortune 500, has revenues that are no less than the revenues of the business entity that ranks 500th in the Fortune 500 list.

1 ~~(B) or the materiality standards in subdivision~~ Subdivision (c)(2) of this regulation if the
2 business entity is listed on the New York Stock Exchange, or if not listed on the New York Stock
3 Exchange, for its most recent fiscal year had earnings before taxes of no less than:

4 ~~(A) \$ 2.5 million, or,~~

5 ~~(B) such other amount described at Rule 102.01C of the New York Stock Exchange's~~
6 ~~Listed Company Manual (or any superseding rule of the New York Stock Exchange describing~~
7 ~~its financial standards for initial listing).~~

8 (c) Indirectly involved business entities. The following materiality standards apply when
9 a business entity in which a public official has an economic interest is indirectly involved in a
10 governmental decision. If more than one of the following subdivisions is applicable to the
11 business entity in question, apply the subdivision with the highest dollar thresholds.

12 (1) If the business entity is listed in the Fortune 500, or, if not listed in the Fortune 500,
13 has revenues that are no less than the revenues of the business entity that ranks 500th in the
14 Fortune 500 list, the financial effect of a governmental decision on the business entity is material
15 if it is reasonably foreseeable that:

16 (A) The governmental decision will result in an increase or decrease in the business
17 entity's gross revenues for a fiscal year of \$ 10,000,000 or more; or

18 (B) The governmental decision will result in the business entity incurring or avoiding
19 additional expenses or reducing or eliminating existing expenses for a fiscal year in the amount
20 of \$ 2,500,000 or more; or

21 (C) The governmental decision will result in an increase or decrease in the value of the
22 business entity's assets or liabilities of \$ 10,000,000 or more.

1 (2) If the business entity is listed on the New York Stock Exchange, or if not listed on the
2 New York Stock Exchange, for its most recent fiscal year had earnings before taxes of no less
3 than \$ 2.5 million, ~~or such other amount described at Rule 102.01C of the New York Stock~~
4 ~~Exchange's Listed Company Manual (or any superseding rule of the New York Stock Exchange~~
5 ~~describing its financial standards for initial listing)~~, the financial effect of a governmental
6 decision on the business entity is material if it is reasonably foreseeable that:

7 (A) The governmental decision will result in an increase or decrease to the business
8 entity's gross revenues for a fiscal year in the amount of \$ 500,000 or more; or,

9 (B) The governmental decision will result in the business entity incurring or avoiding
10 additional expenses or reducing or eliminating existing expenses for a fiscal year in the amount
11 of \$ 200,000 or more; or,

12 (C) The governmental decision will result in an increase or decrease in the value of assets
13 or liabilities of \$ 500,000 or more.

14 (3) If the business entity is listed on either the NASDAQ or American Stock Exchange,
15 or if not so listed, for its most recent fiscal year had: ~~net income of no less than \$ 500,000 (or~~
16 ~~such other amount described in the minimum financial requirements for continued listing on the~~
17 ~~NASDAQ SmallCap market)~~, or earnings before taxes of no less than \$ 750,000 ~~(or such other~~
18 ~~amount of earnings before taxes described under initial listing standard 1 of Section 101(a) of the~~
19 ~~Rules of the American Stock Exchange, or any superseding Section of the Rules of that~~
20 ~~Exchange)~~, the financial effect of a governmental decision on the business entity is material if it
21 is reasonably foreseeable that:

22 (A) The governmental decision will result in an increase or decrease to the business
23 entity's gross revenues for a fiscal year in the amount of \$ 300,000 or more; or,

1 (B) The governmental decision will result in the business entity incurring or avoiding
2 additional expenses or reducing or eliminating existing expenses for a fiscal year in the amount
3 of \$ 100,000 or more; or,

4 (C) The governmental decision will result in an increase or decrease in the value of assets
5 or liabilities of \$ 300,000 or more.

6 (4) If the business entity is not covered by subdivisions (c)(1)-(3), the financial effect of a
7 governmental decision on the business entity is material if it is reasonably foreseeable that:

8 (A) The governmental decision will result in an increase or decrease in the business
9 entity's gross revenues for a fiscal year in the amount of \$ 20,000 or more; or,

10 (B) The governmental decision will result in the business entity incurring or avoiding
11 additional expenses or reducing or eliminating existing expenses for a fiscal year in the amount
12 of \$ 5,000 or more; or,

13 (C) The governmental decision will result in an increase or decrease in the value of the
14 business entity's assets or liabilities of \$ 20,000 or more.

15 (d) Terminology. The accounting terms described below are the same as, or not
16 inconsistent with, terms used in Generally Accepted Accounting Principles and Generally
17 Accepted Auditing Standards. Nothing in this subdivision should be construed to incorporate
18 new items not contemplated under Generally Accepted Accounting Principles and Generally
19 Accepted Auditing Standards, nor to exclude any items that might be included in the definitions
20 of these terms under Generally Accepted Accounting Principles and Generally Accepted
21 Auditing Standards

22 (1) Assets. As used in this section, "assets" means all property, real and personal, tangible
23 and intangible, which belongs to any business entity. This includes, but is not limited to, cash,

1 securities, merchandise, raw materials, finished goods, operating supplies, and ordinary
2 maintenance material and parts, accounts receivable and notes and loans receivable, and prepaid
3 expenses (such as prepaid insurance, interests, rents, taxes, advertising, and operating supplies).

4 (A) When a business entity holds a claim over collateral (including real property) as
5 security for a loan made by the business entity, such a claim does not make the collateral
6 (including real property) an "asset" of the business entity, unless the business entity has initiated
7 proceedings to foreclose upon, or acquire the asset based on the debtor's failure to repay the loan.
8 The loan or note secured by the collateral is an asset.

9 (B) The definition of "assets" also includes intangible assets. Intangible assets, include,
10 but are not limited to, long-lived legal rights and competitive advantages developed or acquired
11 by a business enterprise, patents, copyrights, franchises, trademarks, organizational costs,
12 goodwill, and secret processes.

13 (2) Earnings Before Taxes: Revenue, less the cost of goods sold and selling, general, and
14 administrative expenses (but not excluding depreciation and amortization expenses); otherwise
15 defined as operating and non-operating profit before the deduction of income taxes. Described
16 variously as EBT, Income Before Income Taxes, or Income Before Provision for Income Taxes.

17 (3) Expenses: In general, the term refers to the current costs of carrying on an activity.

18 (4) Gross Revenue: Actual or expected inflows of cash or other assets. "Gross Revenue"
19 is the revenue of a business entity before adjustments or deductions are made for returns and
20 allowances and the costs of goods sold, and prior to any deduction for these and any other
21 expenses.

22 (5) Liabilities: Obligations of the business entity, liquidation of which is reasonably
23 expected to require the transfer of assets or the creation of other new liabilities. Any financial

1 obligation or cash expenditures that must be made by the business entity at a specific time to
2 satisfy the contractual terms of such an obligation.

3 ~~(6) Net Income: A business entity's total earnings; otherwise defined as revenues adjusted~~
4 ~~for the costs of doing business, depreciation, interest, taxes, and other expenses. This amount is~~
5 ~~usually found at the bottom of a business entity's Profit and Loss statement. Also described as~~
6 ~~Net Profit.~~

7 (e) Financial statements. In complying with this regulation, public officials may rely on
8 the most recent independently audited financial statements of the business entity so long as those
9 statements are reflective of the current condition of the business entity. Financial statements are
10 not considered "reflective of the current condition of the business entity" where:

11 (1) The most recent independently audited financial statements of the business entity are
12 for a fiscal year ending more than twenty-four months prior to the date of the governmental
13 decision.

14 (2) The most recent audit of the financial statements resulted in an adverse opinion, was
15 issued with a disclaimer, or was otherwise qualified in such a manner that the statement of assets,
16 liabilities, expenses, or gross revenues is questioned in the audit report, or

17 (3) There has been a subsequent event, intervening between the date that the financial
18 statement was created and the date of the decision of the public official, that makes the statement
19 no longer representative, including, but not limited to, business reorganizations.

20 Comments: Electronic access to annual reports, quarterly reports, and other financial statements
21 filed with the United States Securities and Exchange Commission ("SEC") may be obtained by
22 accessing the SEC's website and selecting its EDGAR database of statutory filings:
23 <http://www.sec.gov/edgar/searchedgar/companysearch.html>.

1 ~~The earnings before taxes and net income criteria for listing on the New York and American~~
2 ~~Stock Exchanges, and NASDAQ may be obtained through links from the following webpages:~~
3 ~~New York Stock Exchange: <http://www.nyse.com/listed/listed.html>.~~
4 ~~American Stock Exchange:~~
5 ~~<http://wallstreet.cch.com/AmericanStockExchangeAMEX/>.~~
6 ~~NASDAQ:~~
7 ~~<http://www.nasdaq.com/about/nasdaq-listing-req-fees.pdf>.~~
8 Note: Authority cited: Section 83112, Government Code. Reference: Sections 87100, 87102.5,
9 87102.6, 87102.8 and 87103